KEEGAN, WERLIN & PABIAN, LLP

ATTORNEYS AT LAW
21 CUSTOM HOUSE STREET
BOSTON, MASSACHUSETTS 02110-3525

(617) 951-1400

TELECOPIERS:
(617) 951-1354
(617) 951-0586

June 12, 2003

Mary L. Cottrell, Secretary
Department of Telecommunications and Energy
One South Station
Boston, MA 02110

Re: D.T.E. 03-47, Boston Edison Company, Cambridge Electric Light Company, Commonwealth Electric Company, NSTAR Gas Company, Pension/PBOP Adjustment Mechanism Tariff Filing, Discovery Responses

Dear Secretary Cottrell:

Enclosed for filing in the above-referenced matter are the responses of Boston Edison Company, Cambridge Electric Light Company, Commonwealth Electric Company and NSTAR Gas Company to the Information Requests set forth on the accompanying list.

Thank you for your attention to this matter.

Sincerely,

Robert N. Werlin /gl

Robert N. Werlin

Enclosures
cc: Service List

Responses to Information Requests

Information Request AG-1-4
Information Request AG-1-5
Information Request AG-1-11
Information Request AG-1-16
Information Request AG-1-17
Information Request AG-1-19
Information Request AG-1-21
Information Request AG-1-35
Information Request AG-1-49
Information Request AG-1-52
Information Request AG-1-53
Information Request AG-1-57

June 12, 2003

Information Request AG-1-4

Please provide the names and titles of each of the Companies' in-house accountants responsible for pension cost accounting for each of the years 1990 through 2002. Please also provide a copy of the curriculum vitae for each of those accountants.

Response

Robert Weafer and Michael Farrell are in-house accountants responsible for pension cost accounting for NSTAR, and before the merger with COM/Energy, Boston Edison. The in-house accountants responsible for pension cost accounting for COM/Energy before the creation of NSTAR are no longer with the Company.

Please see Attachment AG-1-4(a) for a profile of Robert Weafer, Vice President, Controller, and Chief Accounting Officer.

Please see Attachment AG-1-4(b) for a profile of Michael Farrell, Assistant Controller and Director of Accounting.

ROBERT J. WEAFER, JR.

SUMMARY

NSTAR **1975-Present**

VICE PRESIDENT CONTROLLER & CAO **September 1999-Present**
Chief Accounting Officer responsible for the controllership functions of the corporation. These duties include the establishment and monitoring of key accounting and financial practices including accounting, procurement, tax, budgeting and short term financial planning and financial reporting and overall management of the external auditors.

VICE PRESIDENT- FINANCE & CONTROLLER **September 1995-September 1999**
Chief Accounting Officer responsible for all controllership and a significant portion of the treasury functions. Responsibilities included accounting, financial planning and reporting, budgeting, tax, asset management (insurance, facilities, pension, property taxes), corporate finance

VICE PRESIDENT - FOSSIL OPERATIONS **March 1995-September 1995**
Reports to Senior Vice President - Operations. Ran fossil generation business for six months in a unique job rotation assignment.

VICE PRESIDENT, CONTROLLER **1991-March 1995**
CONTROLLER **1983-1991**
Reported to Senior Vice President - Finance. Responsible for accounting, budgeting, supply management, metering, billing, collections, as well as advising CFO on numerous strategic issues.

DIRECTOR OF INTERNAL AUDITING **1975-1983**

PRIOR EXPERIENCE

Grant Thornton, Certified Public Accountants, Boston, MA **1970-1975**

Audit Manager
Responsible for the overall management of financial statement audits in a variety of industries both privately and publicly held. Performed a number of special assignments at the request of clients to improve efficiency and quality of their operations.

EDUCATION

Master in Finance, Bentley College, Waltham, MA
BS, Accounting, Bentley College, Waltham, MA
Certified Public Accountant, Massachusetts

PROFESSIONAL AFFILIATIONS

Financial Executives Institute
American Institute of Certified Public Accountants
Edison Electric Institute
Northeast Gas Association

DIRECTORSHIP

Caritas Norwood Hospital
Yankee Atomic Power Company
Connecticut Yankee Power Company

NSTAR

CANDIDATE PROFILE

Name:	Michael Farrell
Title:	Assistant Controller & Director, Accounting
Business Unit	CFO
Dept/Area:	Controller

Internal Work Experience:

Position: Assistant Controller & Director Accounting (NSTAR)	**1999 - present**
Dept/Div: Controller	
Major Responsibilities: Responsible for the accounting for all NSTAR companies, including the Payroll and Fixed Asset Accounting Departments. This includes timely and accurate monthly closings, compliance with accounting and regulatory standards, analysis of financial results and maintenance of the company's general ledger.	

Position: Assistant Controller (Boston Edison)	**1996 - 1999**
Dept/Div: Finance & Accounting	
Major Responsibilities **Responsible for all of the accounting for Boston Edison and the consolidation of BEC Energy. This included Financial Reporting, General Ledger and Plant Accounting. For approximately 1 year of this time, I was also responsible for the company's Operating Plan and budgeting process.**	

Position: Team Leader, Financial Reports (Boston Edison)	**1996**
Dept/Div: Finance & Accounting	
Major Responsibilities: Responsible for the external and management financial reporting of the company.	

External Work Experience:

Company: New England Electric System	**1994 - 1995**
Position: Senior Financial Analyst	
Major Responsibilities: Responsible for the revenue requirements of Massachusetts Electric Co. Testified before the DTE in public hearings in general rate case and purchased power clause case. Assisted other personnel in rate proceedings of other retail companies and New England Power.	

Company Coopers & Lybrand	**1987 - 1994**
Position: Business Assurance Manager	
Major Responsibilities: Over saw the audits of a variety of clients including: public utilities, registered investment companies and securities broker/dealers. This included the adherence to GAAP and the maintenance of internal accounting controls. Special projects included consulting with the MWRA Advisory Board on wholesale Sewer rates (project included presentations before the board, public hearings and the Mass. Legislature).	

Education:

Institution	Major	Degree	Year
Bentley College	Accountancy	B.S.	1987

Licenses and Certifications

License/Certificate	Date Received
Certified Public Accountant	12/6/90

Professional Associations:

Massachusetts Society of Certified Public Accountants
Edison Electric Institute Corporate Accounting Committee

Information Request AG-1-5

Please provide the names and titles of each of the Companies' in-house accountants responsible for post-retirement benefits other than pension cost accounting for each of the years 1990 through 2002. Please also provide a copy of the curriculum vitae for each of those accountants.

Response

The Accountants responsible for COM/Energy's post-retirement benefits other than pension accounting prior to the formation of NSTAR are no longer with the Company.

SFAS 106 was effective beginning in 1993. From 1993 to the present, Robert J. Weafer has been the Controller of Boston Edison and NSTAR (since the merger). Since 1996, Michael F. Farrell has been Assistant Controller of Boston Edison and NSTAR (since the merger). Messrs. Weafer and Farrell are both Certified Public Accountants and are responsible for the post-retirement benefits other than pension accounting at NSTAR. Please see the Attachments AG-1-4(a) and AG-1-4(b) for their professional experience.

Information Request AG-1-11

Please provide the contribution by each of the Companies to each of the pension trust funds for each of the years 1990 through 2003.

Response

Please see the Company's response to Information Request DTE-1-2 for information regarding pension contributions for 1993 through 2003.

The following contributions were made to the pension trust funds during 1990 through 1992:

Company	1990	1991	1992
Boston Edison	$3,615,000	$0	$0
Commonwealth Electric	$3,693,000	$4,082,000	$3,679,000
Cambridge	$546,000	$571,000	$494,000
Commonwealth Gas	$2,460,000	$2,482,000	$2,136,000

Information Request AG-1-16

Please provide the amount of pension expense that each of the Companies used as a tax deduction on its federal income tax filings for each of the years 1990 through 2002.

Response

The pension contributions included in the Companies tax returns for 1990 to 2002 are listed below. Both COM/Energy and NSTAR filed consolidated Federal income tax returns, and therefore, the information cannot be provided separately for each individual subsidiary. In addition, the contribution amounts on each year's tax return may not necessary correspond to that year's actual cash contributions. For accounting purposes, contributions are reflected in the calendar year of the contribution. For purpose of the minimum and maximum contributions for tax purposes, contributions can be made up until the filing of the tax return (9/15 of the following year). Also, contributions may be carried back to previous years when the maximum contribution is not met.

	NSTAR	Boston Edison	Com/Energy	Total
1990	-	-	5,554,000	5,554,000
1991	-	-	8,628,000	8,628,000
1992	-	-	5,359,000	5,359,000
1993	-	5,034,000	8,126,000	13,160,000
1994	-	24,974,000	8,421,000	33,395,000
1995	-	45,057,000	14,267,000	59,324,000
1996	-	55,000,000	8,777,000	63,777,000
1997	-	25,000,000	5,196,000	30,196,000
1998	-	85,000,000	5,455,000	90,455,000
1999	-	73,000,000	27,610,000	100,610,000
2000	5,250,000	-	-	5,250,000
2001	55,750,000	-	-	55,750,000
2002	49,500,000	-	-	49,500,000
	110,500,000	313,065,000	97,393,000	520,958,000

Information Request AG-1-17

Please provide the amount of post-retirement benefits other than pensions expense that each of the Companies used as a tax deduction on its federal income tax filings for each of the years 1990 through 2002.

Response

The pension contributions included in the Companies tax returns for 1993 to 2002 are listed below. Information prior to 1993 is not applicable, because VEBAs were not maintained for the purpose of funding those benefits prior to that date. Both COM/Energy and NSTAR filed consolidated Federal income tax returns, and therefore, the information cannot be provided separately for each individual subsidiary.

	NSTAR	Boston Edison	Com/Energy	Total
1993	-	18,000,000	15,822,000	33,822,000
1994	-	25,034,000	14,460,000	39,494,000
1995	-	21,946,000	13,972,000	35,918,000
1996	-	26,134,000	13,698,000	39,832,000
1997	-	23,229,000	12,152,000	35,381,000
1998	-	8,959,000	11,697,000	20,656,000
1999	-	9,880,000	11,707,000	21,587,000
2000	63,460,000	0	0	63,460,000
2001	39,722,000	0	0	39,722,000
2002	38,500,000	0	0	38,500,000
	141,682,000	133,182,000	93,508,000	368,372,000

Information Request AG-1-19

Please provide copies of the post-retirement benefits other than pensions trust fund financial statements for each of the Companies for each of the years 1990 through 2002.

Response

All plans' assets are held in a Voluntary Employees' Beneficiary Association trust pursuant to Section 501 (c)(9) of the Internal Revenue Code. All plans were required to adopt the Statement of Position 92-6, "accounting and Reporting by Health and Welfare Benefits Plans" beginning in 1993. Prior to 1993, the Companies reported retiree health care and life insurance benefits under the traditional "pay-as-you-go" method and reported their annual expense as a footnote in their respective Form 10-Ks.

Reports for the years 1993 – 1999 are being provided for both Boston Edison and Commonwealth Energy System. Commonwealth Energy System has three reports for each year: Postretirement Benefit Plan – Group I (represented employees); Postretirement Benefit Plan – Group II (non-represented employees); and Postretirement Life Insurance Benefit Plan (all employees)

Beginning in 2000, a single annual report was produced for NSTAR. The report for 2002 has not been published at this time. The reports are provided herewith as Attachment AG-1-19.

Please note that the attachments are bulk documents and are therefore being provided only to the Secretary, the Hearing Officer and the Attorney General. A copy of each is also available for inspection at the Company's offices during normal business hours.

Information Request AG-1-21

Please provide logs of all meetings and telephone calls with the Department regarding the deferral of pension and post-retirement benefits other than pensions costs.

Response

The Company does not have written logs of meetings and telephone calls that are responsive to this question. However, Company personnel met with Department Staff on November 20, 2003 and with Staff and Commissioners on November 22, 2002, prior to the Company's November 27, 2002 letter requesting an accounting ruling. The Department Staff convened a conference call with Company personnel on December 18, 2002, to ask certain procedural and technical questions.

Information Request AG-1-35

Referring to the proposed Boston Edison Company Tariff, page 1, Section 1.01, please provide a complete and detailed description of the term "SFAS 106." Please also provide all supporting documentation for that description.

Response

"SFAS 106" refers to Statement of Financial Accounting Standards No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions." Statements of Financial Accounting Standards are issued by the Financial Accounting Standards Board ("FASB"). SFAS 106 is oftentimes referred to as FASB 106 or FAS 106. Please see Attachment AG-1-35 for a copy of SFAS 106. SFAS 132 amended reporting requirements for SFAS 106. A copy of SFAS 132 is provided as Attachment AG-1-34(b).

D.T.E. 03-47
Attachment AG-1-35

Browse Location: United States\Financial Accounting Standards Board (FASB)\Original Pronouncements\FASB Statements (FAS)\FAS 101 to 125 (Issued Dec 1988 - Dec 1996)\FAS 106: Employers' Accounting for Postretirement Benefits Other Than Pensions
Publish Date: 11 October, 2002

FAS 106: Employers' Accounting for Postretirement Benefits Other Than Pensions

FAS 106 STATUS

Issued:	December 1990
Effective Date:	For fiscal years beginning after December 15, 1992
Affects:	Amends APB 12, paragraph 6 Supersedes APB 12, footnote 1 Amends APB 16, paragraph 88 Supersedes FAS 81 Amends FAS 87, paragraph 8 Supersedes FAS 87, footnote 3 Supersedes FTB 87-1
Affected by:	Paragraph 65 amended by FAS 135 Paragraphs 74, 77, 78, 82, 106, and 479 through 483 superseded by FAS 132 Paragraph 86 and 444 amended by FAS 141 Paragraph 96(a) amended by FAS 144 Paragraphs 103, 107, 392, 417, and 461 amended by FAS 135 Paragraph 103 superseded by FAS 144 Paragraphs 464, 467, and 471 superseded by FAS 135 Footnote 23 superseded by FAS 135
Other Interpretive Releases:	FASB Special Report, *A Guide to Implementation of Statement 106 on Employers' Accounting for Postretirement Benefits Other Than Pensions: Questions and Answers* FASB Special Report, *A Guide to Implementation of Statement 87 on Employers' Accounting for Pensions: Questions and Answers* FASB Special Report, *A Guide to Implementation of Statement 88 on Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits: Questions and Answers*

Note: Although the Special Reports for Statements 87 and 88 do not specifically refer to postretirement benefits other than pensions, the user is referred to them because of the similarity in accounting.

Issues Discussed by FASB Emerging Issues Task Force (EITF)

Affects:	Nullifies EITF Issue No. 86-20 Partially resolves EITF Issue No. 84-35 Resolves EITF Issue No. 86-19
Interpreted by:	Paragraph 105 interpreted by EITF Issue No. 86-27 Paragraph 186 interpreted by EITF Topic No. D-36 Paragraphs 308 and 518 interpreted by EITF Issue No. 93-3
Related Issues:	EITF Issues No. 88-23, 92-12, 92-13, and 96-5 and Topics No. D-27 and D-92

FAS 106 Summary

This Statement establishes accounting standards for employers' accounting for postretirement benefits other than pensions (hereinafter referred to as postretirement benefits). Although it applies to all forms of postretirement benefits, this Statement focuses principally on postretirement health care benefits. It will significantly change the prevalent current practice of accounting for postretirement benefits on a pay-as-you-go (cash) basis by requiring accrual, during the years that the employee renders the necessary service, of the expected cost of providing those benefits to an employee and the employee's beneficiaries and covered dependents.

The Board's conclusions in this Statement result from the view that a defined postretirement benefit plan sets forth the terms of an exchange between the employer and the employee. In exchange for the current services provided by the employee, the employer promises to provide, in addition to wages and other benefits, health and other welfare benefits after the employee retires. It follows from that view that postretirement benefits are not gratuities but are part of an employee's compensation for services rendered. Since payment is deferred, the benefits are a type of deferred compensation. The employer's obligation for that compensation is incurred as employees render the services necessary to earn their postretirement benefits.

The ability to measure the obligation for postretirement health care benefits and the recognition of that obligation have been the subject of controversy. The Board believes that measurement of the obligation and accrual of the cost based on best estimates are superior to implying, by a failure to accrue, that no obligation exists prior to the payment of benefits. The Board believes that failure to recognize an obligation prior to its payment impairs the usefulness and integrity of the employer's financial statements.

The Board's objectives in issuing this Statement are to improve employers' financial reporting for postretirement benefits in the following manner:

a. To enhance the relevance and representational faithfulness of the employer's reported results of operations by recognizing net periodic postretirement benefit cost as employees render the services necessary to earn their postretirement benefits

b. To enhance the relevance and representational faithfulness of the employer's statement of financial position by including a measure of the obligation to provide postretirement benefits based on a mutual understanding between the employer and its employees of the terms of the underlying plan

c. To enhance the ability of users of the employer's financial statements to understand the extent and effects of the employer's undertaking to provide postretirement benefits to its employees by disclosing relevant information about the obligation and cost of the postretirement benefit plan and how those amounts are measured

d. To improve the understandability and comparability of amounts reported by requiring employers with similar plans to use the same method to measure their accumulated postretirement benefit obligations and the related costs of the postretirement benefits.

Similarity to Pension Accounting

The provisions of this Statement are similar, in many respects, to those in FASB Statements No. 87, *Employers' Accounting for Pensions*, and No. 88, *Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits.* To the extent the promise to provide pension benefits and the promise to provide postretirement benefits are similar, the provisions of this Statement are similar to those prescribed by Statements 87 and 88; different accounting treatment is prescribed only when the Board has concluded that there is a compelling reason for different treatment. Appendix B identifies the major similarities and differences between this Statement and employers' accounting for pensions.

Basic Tenets

This Statement relies on a basic premise of generally accepted accounting principles that accrual accounting provides more relevant and useful information than does cash basis accounting. The importance of information about cash flows or the funding of the postretirement benefit plan is not ignored. Amounts funded or paid are given accounting recognition as uses of cash, but the Board believes that information about cash flows alone is insufficient. Accrual accounting goes beyond cash transactions and attempts to recognize the financial effects of noncash transactions and events as they occur. Recognition and measurement of the accrued obligation to provide postretirement benefits will provide users of financial statements with the opportunity to assess the financial consequences of employers' compensation decisions.

In applying accrual accounting to postretirement benefits, this Statement adopts three fundamental aspects of pension accounting: delayed recognition of certain events, reporting net cost, and offsetting liabilities and related assets.

Delayed recognition means that certain changes in the obligation for postretirement benefits, including those changes arising as a result of a plan initiation or amendment, and certain changes in the value of plan assets set aside to meet that obligation are not recognized as they occur. Rather, those changes are recognized systematically over future periods. All changes in the obligation and plan assets ultimately are recognized unless they are first reduced by other changes. The changes that have been identified and quantified but not yet recognized in the employer's financial statements as components of net periodic postretirement benefit cost and as a liability or asset are disclosed.

Net cost means that the recognized consequences of events and transactions affecting a postretirement benefit plan are reported as a single amount in the employer's financial statements. That single amount includes at least three types of events or transactions that might otherwise be reported separately. Those events or transactions-exchanging a promise of deferred compensation in the form of postretirement benefits for employee service, the interest cost arising from the passage of time until those benefits are paid, and the returns from the investment of plan assets-are disclosed separately as components of net periodic postretirement benefit cost.

Offsetting means that plan assets restricted for the payment of postretirement benefits offset the accumulated postretirement benefit obligation in determining amounts recognized in the employer's statement of financial position and that the return on those plan assets offsets postretirement benefit cost in the employer's statement of income. That offsetting is reflected even though the obligation has not been settled, the investment of the plan assets may be largely controlled by the employer, and substantial risks and rewards associated with both the obligation and the plan assets are borne by the employer.

Recognition and Measurement

The Board is sensitive to concerns about the reliability of measurements of the postretirement health care benefit obligation. The Board recognizes that limited historical data about per capita claims costs are available and that actuarial practice in this area is still developing. The Board has taken those factors into consideration in its decisions to delay the effective date for this Statement, to emphasize disclosure, and to permit employers to phase in recognition of the transition obligation in their statements of financial position. However, the Board believes that those factors are insufficient reason not to use accrual accounting for postretirement benefits in financial reporting. With increased experience, the reliability of measures of the obligation and cost should improve.

An objective of this Statement is that the accounting reflect the terms of the exchange transaction that takes place between an employer that provides postretirement benefits and the employees who render services in exchange for those benefits. Generally the extant written plan provides the best evidence of that exchange transaction. However, in some situations, an employer's cost-sharing policy, as evidenced by past practice or by communication of intended changes to a plan's cost-sharing provisions, or a past practice of regular increases in certain monetary benefits may indicate that the substantive plan-the plan as understood by the parties to the exchange transaction-differs from the extant written plan. The substantive plan is the basis for the accounting.

This Statement requires that an employer's obligation for postretirement benefits expected to be provided to or for an employee be fully accrued by the date that employee attains full eligibility for all of the benefits expected to be received by that employee, any beneficiaries, and covered dependents (the full eligibility date), even if the employee is expected to render additional service beyond that date. That accounting reflects the fact that at the full eligibility date the employee has provided all of the service necessary to earn the right to receive all of the benefits that employee is expected to receive under the plan.

The beginning of the attribution (accrual) period is the employee's date of hire unless the plan only grants credit for service from a later date, in which case benefits are generally attributed from the beginning of that credited service period. An equal amount of the expected postretirement benefit obligation is attributed to each year of service in the attribution period unless the plan attributes a disproportionate share of the expected benefits to employees' early years of service. The Board concluded that, like accounting for other deferred compensation agreements, accounting for postretirement benefits should reflect the explicit or implicit contract between the employer and its employees.

Single Method

The Board believes that understandability, comparability, and usefulness of financial information are improved by narrowing the use of alternative accounting methods that do not reflect different facts and circumstances. The Board has been unable to identify circumstances that would make it appropriate for different employers to use fundamentally different accounting methods or measurement techniques for similar postretirement benefit plans or for a single employer to use fundamentally different methods or measurement techniques for different plans. As a result, a single method is prescribed for measuring and recognizing an employer's accumulated postretirement benefit obligation.

Amendment to Opinion 12

An employer's practice of providing postretirement benefits to selected employees under individual contracts, with specific terms determined on an individual-by-individual basis, does not constitute a postretirement benefit *plan* under this Statement. This Statement amends APB Opinion No. 12, *Omnibus Opinion-1967,* to explicitly require that an employer's obligation under deferred compensation contracts be accrued following the terms of the individual contract over the required service periods to the date the employee is fully eligible for the benefits.

Transition

Unlike the effects of most other accounting changes, a transition obligation for postretirement benefits generally reflects, to a considerable extent, the failure to accrue the accumulated postretirement benefit obligation in earlier periods as it arose rather than the effects of a change from one acceptable accrual method of accounting to another. The Board believes that accounting for transition from one method of accounting to another is a practical matter and that a major objective of that accounting is to minimize the cost and mitigate the disruption to the extent possible without unduly compromising the ability of financial statements to provide useful information.

This Statement measures the transition obligation as the unfunded and unrecognized accumulated postretirement benefit obligation for all plan participants. Two options are provided for recognizing that transition obligation. An employer can choose to immediately recognize the transition obligation as the effect of an accounting change, subject to certain limitations. Alternatively, an employer can choose to recognize the transition obligation in the statement of financial position and statement of income on a delayed basis over the plan participants' future service periods, with disclosure of the unrecognized amount. However, that delayed recognition cannot result in less rapid recognition than accounting for the transition obligation on a pay-as-you-go basis.

Effective Dates

This Statement generally is effective for fiscal years beginning after December 15, 1992, except that the application of this Statement to plans outside the United States and certain small, nonpublic employers is delayed to fiscal years beginning after December 15, 1994. The amendment of Opinion 12 is effective for fiscal years beginning after March 15, 1991.

* * *

The Board appreciates the contributions of the many people and organizations that assisted the Board in its research on this project.

INTRODUCTION

1. This Statement establishes standards of financial accounting and reporting for an employer that offers **postretirement benefits other than pensions** [1] (hereinafter referred to as **postretirement benefits**) to its employees.[2] The Board added a project on postemployment **benefits** other than pensions to its agenda in 1979 as part of its project on accounting for pensions and other postemployment benefits. In 1984, the subject of accounting for postemployment benefits other than pensions was identified as a separate project. As interim measures, FASB Statement No. 81, *Disclosure of Postretirement Health Care and Life Insurance Benefits,* was issued in November 1984, and FASB Technical Bulletin No. 87-1, *Accounting for a Change in Method of Accounting for Certain Postretirement Benefits,* was issued in April 1987.

2. Most employers have accounted for postretirement benefits on a pay-as-you-go (cash) basis. As the prevalence and magnitude of employers' promises to provide those benefits have increased, there has been increased concern about the failure of financial reporting to identify the financial effects of those promises.

3. The Board views a **postretirement benefit plan** as a deferred compensation arrangement whereby an employer promises to exchange future benefits for employees' current services. Because the obligation to provide benefits arises as employees render the services necessary to earn the benefits pursuant to the terms of the **plan,** the Board believes that the cost of providing the benefits should be recognized over those employee service periods.

4. This Statement addresses, for the first time, the accounting issues related to measuring and recognizing the exchange that takes place between an employer that provides postretirement benefits and the employees who render services in exchange for those benefits. The Board believes the accounting recognition required by this Statement should result in more useful and representationally faithful financial statements. However, this Statement is not likely to be the final step in the evolution of more useful accounting for postretirement benefit arrangements.

5. The Board's objectives in issuing this Statement are to improve employers' financial reporting for postretirement benefits in the following manner:

a. To enhance the relevance and representational faithfulness of the employer's reported results of operations by recognizing **net periodic postretirement benefit cost** [3] as employees render the services necessary to earn their postretirement benefits

b. To enhance the relevance and representational faithfulness of the employer's statement of financial position by including a measure of the obligation to provide postretirement benefits based on a mutual understanding between the employer and its employees of the terms of the underlying plan

c. To enhance the ability of users of the employer's financial statements to understand the extent and effects of the employer's undertaking to provide postretirement benefits to its employees by disclosing relevant information about the obligation and cost of the postretirement benefit plan and how those amounts are measured

d. To improve the understandability and comparability of amounts reported by requiring employers with similar plans to use the same method to measure their **accumulated postretirement benefit obligations** and the related costs of the postretirement benefits.

STANDARDS OF FINANCIAL ACCOUNTING AND REPORTING

Scope

6. This Statement applies to *all* postretirement benefits expected to be provided by an employer to current and former employees (including **retirees**, disabled employees,[4] and other former employees who are expected to receive postretirement benefits), their beneficiaries, and covered dependents, pursuant to the terms of an employer's undertaking to provide those benefits. Postretirement benefits include, but are not limited to, postretirement health care;[5] life insurance provided outside a pension plan to retirees; and other welfare benefits such as tuition assistance, day care, legal services, and housing subsidies provided after retirement. Often those benefits are in the form of a reimbursement to plan participants or direct payment to providers for the cost of specified services as the need for those services arises, but they may also include benefits payable as a lump sum, such as death benefits. This Statement also applies to **settlement** of all or a part of an employer's accumulated postretirement benefit obligation or **curtailment** of a postretirement benefit plan and to an employer that provides postretirement benefits as part of a special **termination benefits** offer.

7. For the purposes of this Statement, a postretirement benefit plan is an arrangement that is mutually understood by an employer and its employees, whereby an employer undertakes to provide its current and former employees with benefits after they retire in exchange for the employees' services over a specified period of time, upon attaining a specified age while in service, or both. Benefits may commence immediately upon termination of service or may be deferred until retired employees attain a specified age.

8. An employer's practice of providing postretirement benefits may take a variety of forms and the obligation may or may not be funded. This Statement applies to any arrangement that is in substance a postretirement benefit plan, regardless of its form or the means or timing of its funding. This Statement applies both to written plans and to unwritten plans whose existence is discernible either from a practice of paying postretirement benefits or from oral representations made to current or former employees. Absent evidence to the contrary, it shall be presumed that an employer that has provided postretirement benefits in the past or is currently promising those benefits to employees will continue to provide those future benefits.

9. This Statement applies to deferred compensation contracts with individual employees if those contracts, taken together, are equivalent to a plan that provides postretirement benefits. It does not apply to an employer's practice of providing postretirement benefits to selected employees under individual contracts with specific terms determined on an individual-by-individual basis. Those contracts shall be accounted for individually, following the terms of the contract. To the extent the contract does not attribute the benefits to individual years of service, the expected future benefits should be accrued over the period of service required to be rendered in exchange for the benefits. (Refer to paragraph 13.)

10. A postretirement benefit plan may be part of a larger plan or arrangement that provides benefits currently to active employees as well as to retirees. In those circumstances, the promise to provide benefits to present and future retirees under the plan shall be segregated from the promise to provide benefits currently to active employees and shall be accounted for in accordance with the provisions of this Statement.

11. This Statement does not apply to pension or life insurance benefits provided through a pension plan. The accounting for those benefits is set forth in FASB Statements No. 87, *Employers' Accounting for Pensions,* and No. 88, *Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits.*[6]

12. This Statement supersedes FASB Statement No. 81, *Disclosure of Postretirement Health Care and Life Insurance Benefits.* Paragraphs 13 and 114 of this Statement amend APB Opinion No. 12, *Omnibus Opinion-1967;* paragraph 14 amends Statement 87; and paragraph 89 amends APB Opinion No. 16, *Business Combinations.* Paragraph 115 rescinds FASB Technical Bulletin No. 87-1, *Accounting for a Change in Method of Accounting for Certain Postretirement Benefits.*

Amendment to Opinion 12

13. The following paragraphs and footnote replace the first four sentences and footnote of paragraph 6 of Opinion 12:

> FASB Statement No. 87, *Employers' Accounting for Pensions,* or Statement No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions,* applies to deferred compensation contracts with individual employees if those contracts, taken together, are equivalent to a postretirement income plan or a postretirement health or welfare benefit plan, respectively. Other deferred compensation contracts shall be accounted for individually on an accrual basis in accordance with the terms of the underlying contract.
>
> To the extent the terms of the contract attribute all or a portion of the expected future benefits to an individual year of the employee's service, the cost of those benefits shall be recognized in that year. To the extent the terms of the contract attribute all or a portion of the expected future benefits to a period of service greater than one year, the cost of those benefits shall be accrued over that period of the employee's service in a systematic and rational manner. At the end of that period the aggregate amount accrued shall equal the then present value of the benefits expected to be provided to the employee, any beneficiaries, and covered dependents in exchange for the employee's service to that date.
>
> *The amounts to be accrued periodically shall result in an accrued amount at the full eligibility date (as defined in Statement 106) equal to the then present value of all of the future benefits expected to be paid. Paragraphs 413-416 of Statement 106 illustrate application of this paragraph.

Amendment to Statement 87

14. The following sentences replace the first two sentences and footnote of paragraph 8 of Statement 87:

> This Statement does not apply to life insurance benefits provided outside a pension plan or to other postretirement health and welfare benefits. The accounting for those benefits is set forth in FASB Statement No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions.*

Use of Reasonable Approximations

15. This Statement is intended to specify accounting objectives and results rather than computational means of obtaining those results. If estimates, averages, or computational shortcuts can reduce the cost of applying this Statement, their use is appropriate, provided the results are reasonably expected not to be materially different from the results of a detailed application.

Single-Employer Defined Benefit Postretirement Plans

16. This Statement primarily focuses on an employer's accounting for a **single-employer plan** that defines the postretirement benefits to be provided to retirees. For purposes of this Statement, a **defined benefit postretirement plan** is one that defines the postretirement benefits in terms of (a) monetary amounts (for example, $100,000 of life insurance) or (b) benefit coverage to be provided (for example, up to $200 per day for hospitalization, 80 percent of the cost of specified surgical procedures, and so forth). (Specified monetary amounts and benefit coverage are hereinafter collectively referred to as *benefits*.)

17. In some cases, an employer may limit its obligation through an individual or an aggregate "cap" on the employer's cost or benefit obligation. For example, an employer may elect to limit its annual postretirement benefit obligation for each retired plan participant to a maximum of $5,000. Or, an employer may elect to limit its share of the aggregate cost of covered postretirement health care benefits for a period to an amount determined based on an average per capita cost per retired plan participant. Plans of that nature are considered to be defined benefit postretirement plans. Paragraphs 472-478 illustrate measurement considerations for defined-dollar capped plans.

18. A postretirement benefit is part of the compensation paid to an employee for services rendered. In a defined benefit plan, the employer promises to provide, in addition to current wages and benefits, future benefits during retirement. Generally, the amount of those benefits depends on the **benefit formula** (which may include factors such as the number of years of service rendered or the employee's compensation before retirement or termination), the longevity of the retiree and any beneficiaries and covered dependents, and the incidence of events requiring benefit payments (for example, illnesses affecting the amount of health care required). In most cases, services are rendered over a number of years before an employee retires and begins to receive benefits or is entitled to receive benefits as a need arises. Even though the services rendered by the employee are complete and the employee has retired, the total amount of benefits the employer has promised and the cost to the employer of the services rendered are not precisely determinable but can be estimated using the plan's benefit formula and estimates of the effects of relevant future events.

Basic Elements of Accounting for Postretirement Benefits

19. Any method of accounting that recognizes the cost of postretirement benefits over employee service periods (before the payment of benefits to retirees) must deal with two factors that stem from the nature of the arrangement. First, estimates or **assumptions** must be made about the future events that will determine the amount and timing of the benefit payments. Second, an **attribution** approach that assigns benefits and the cost of those benefits to individual years of service must be selected.

20. The **expected postretirement benefit obligation** for an employee is the **actuarial present value** as of a particular date of the postretirement benefits expected to be paid by the employer's plan to or for the employee, the employee's beneficiaries, and any covered dependents pursuant to the terms of the plan. Measurement of the expected postretirement benefit obligation is based on the expected amount and timing of future benefits, taking into consideration the expected future cost of providing the benefits and the extent to which those costs are shared by the employer, the employee (including consideration of contributions required during the employee's active service period and following retirement, deductibles, coinsurance provisions, and so forth), or others (such as through governmental programs).

21. The accumulated postretirement benefit obligation [7] as of a particular date is the actuarial present value of all future benefits attributed to an employee's service rendered to that date pursuant to paragraphs 43 and 44 and 52-55, assuming the plan continues in effect and that all assumptions about future events are fulfilled. Prior to the date on which an employee attains **full eligibility** for the benefits that employee is expected to earn under the terms of the postretirement benefit plan (the **full eligibility date**), the accumulated postretirement benefit obligation for an employee is a portion of the expected postretirement benefit obligation. On and after the full eligibility date, the accumulated postretirement benefit obligation and the expected postretirement benefit obligation for an employee are the same. Determination of the full eligibility date is affected by plan terms that provide incremental benefits expected to be received by or on behalf of an employee for additional years of service, unless those incremental benefits are Determination of the full eligibility date is not affected by plan terms that define when benefit payments commence or by an employee's current **dependency status.** (Paragraphs 397-408 illustrate determination of the full eligibility date.)

22. Net periodic postretirement benefit cost comprises several components that reflect different aspects of the employer's financial arrangements. The **service cost** component of net periodic postretirement benefit cost is the actuarial present value of benefits attributed to services rendered by employees during the period (the portion of the expected postretirement benefit obligation attributed to service in the period). The service cost component is the same for an unfunded plan, a plan with minimal funding, and a well-funded plan. The other components of net periodic postretirement benefit cost are **interest cost** [8] (interest on the accumulated postretirement benefit obligation, which is a discounted amount), **actual return on plan assets**, **amortization** of **unrecognized prior service cost**, amortization of the **transition obligation** or **transition asset**, and the **gain or loss component.**

Measurement of Cost and Obligations

Accounting for the Substantive Plan

23. An objective of this Statement is that the accounting reflect the terms of the exchange transaction that takes place between an employer that provides postretirement benefits and the employees who render services in exchange for those benefits, as those terms are understood by both parties to the transaction. Generally, the extant written plan provides the best evidence of the terms of that exchange transaction. However, in some situations, an employer's **cost-sharing** policy, as evidenced by past practice or by communication of intended changes to a plan's cost-sharing provisions (paragraphs 24 and 25), or a past practice of regular increases in certain monetary benefits (paragraph 26) may indicate that the **substantive plan**-the plan as understood by the parties to the exchange transaction-differs from the extant written plan. The substantive plan shall be the basis for the accounting.

24. Except as provided in paragraph 25, an employer's cost-sharing policy, as evidenced by the following past practice or communication, shall constitute the cost-sharing provisions of the substantive plan if either of the following conditions exist. Otherwise, the extant written plan shall be considered to be the substantive plan.

a. The employer has a past practice of (1) maintaining a consistent level of cost sharing between the employer and its retirees through changes in deductibles, coinsurance provisions, retiree contributions, or some combination of those changes or (2) consistently increasing or reducing the employer's share of the cost of the covered benefits through changes in retired or **active plan participants'** contributions toward their retiree health care benefits, deductibles, coinsurance provisions, out-of-pocket limitations, and so forth, in accordance with the employer's established cost-sharing policy

b. The employer has the ability, and has communicated to affected **plan participants** its intent, to institute different cost-sharing provisions at a specified time or when certain conditions exist (for example, when health care cost increases exceed a certain level).

25. An employer's past practice of maintaining a consistent level of cost sharing with its retirees or consistently increasing or reducing its share of the cost of providing the covered benefits shall not constitute provisions of the substantive plan if accompanied by identifiable offsetting changes in other benefits or compensation [9] or if the employer incurred significant costs, such as work stoppages, to effect that cost-sharing policy.[10] Similarly, an employer's communication of its intent to institute cost-sharing provisions that differ from the extant written plan or the past cost-sharing practice shall not constitute provisions of the substantive plan (a) if the plan participants would be unwilling to accept the change without adverse consequences to the employer's operations or (b) if other modifications of the plan, such as the level of benefit coverage, or providing offsetting changes in other such as pension benefits, would be required to gain plan participants' acceptance of the change to the cost-sharing arrangement.

26. A past practice of regular increases in postretirement benefits defined in terms of monetary amounts may indicate that the employer has a present commitment to make future *improvements* to the plan and that the plan will provide monetary benefits attributable to prior service that are greater than the monetary benefits defined by the extant written plan. In those situations, the substantive commitment to increase those benefits shall be the basis for the accounting. Changes in the benefits, other than benefits defined in terms of monetary amounts, covered by a postretirement health care plan or by other postretirement benefit plans shall not be anticipated.

27. Contributions expected to be received from active employees toward the cost of their postretirement benefits and from retired plan participants are treated similarly for purposes of measuring an employer's expected postretirement benefit obligation. That obligation is measured as the actuarial present value of the benefits expected to be provided under the plan, reduced by the actuarial present value of contributions expected to be received from the plan participants during their remaining active service and postretirement periods. In determining the amount of the contributions expected to be received from those participants toward the cost of their postretirement benefits, consideration is given to any related substantive plan provisions, such as an employer's past practice of consistently increasing or reducing the contribution rates as described in paragraphs 24 and 25. An obligation to return contributions received from employees who do not attain eligibility for postretirement benefits and, if applicable, any interest accrued on those contributions shall be recognized as a component of an employer's postretirement benefit obligation.

28. Automatic benefit changes [11] specified by the plan that are expected to occur shall be included in measurements of the expected and accumulated postretirement benefit obligations and the service cost component of net periodic postretirement benefit cost. Also, **plan amendments** shall be included in the computation of the expected and accumulated postretirement benefit obligations once they have been contractually agreed to, even if some provisions take effect only in future periods. For example, if a plan amendment grants a different benefit level for employees retiring after a future date, that increased or reduced benefit level shall be included in current-period measurements for employees expected to retire after that date.

Assumptions

29. The Board believes that measuring the net periodic postretirement benefit cost and accumulated postretirement benefit obligation based on best estimates is superior to implying, by a failure to accrue, that no cost or obligation exists prior to the payment of benefits. This Statement requires the of **explicit assumptions,** each of which individually represents the best estimate of a particular future event, to measure the expected postretirement benefit obligation. A portion of that expected postretirement benefit obligation is attributed to each period of an employee's service associated with earning the postretirement benefits, and that amount is accrued as service cost for that period.

30. The service cost component of postretirement benefit cost, any **prior service cost,** and the accumulated postretirement benefit obligation are measured using actuarial assumptions and present value techniques to calculate the actuarial present value of the expected future benefits attributed to periods of employee service. Each assumption used shall reflect the best estimate solely with respect to that individual assumption. All assumptions shall presume that the plan will continue in effect in the absence of evidence that it will not continue. Principal actuarial assumptions include the time value of money (**discount rates**); participation rates (for **contributory plans**); retirement age; factors affecting the amount and timing of benefit payments, which for **postretirement health care benefits** consider past and present **per capita claims cost by age, health care cost trend rates, Medicare reimbursement rates,** and so forth; salary progression (for **pay-related plans**); and the probability of payment (turnover, dependency status, mortality, and so forth).

31. Assumed discount rates shall reflect the time value of money as of the **measurement date** in determining the present value of future cash outflows currently expected to be required to satisfy the postretirement benefit obligation. In making that assumption, employers shall look to rates of return on high-quality fixed-income investments currently available whose cash flows match the timing and amount of expected benefit payments. If settlement of the obligation with third-party insurers is possible (for example, the purchase of nonparticipating life insurance contracts to provide death benefits), the interest rates inherent in the amount at which the postretirement benefit obligation could be settled are relevant in determining the assumed discount rates. Assumed discount rates are used in measurements of the expected and accumulated postretirement benefit obligations and the service cost and interest cost components of net periodic postretirement benefit cost.

32. The **expected long-term rate of return on plan assets** shall reflect the average rate of earnings expected on the existing assets that qualify as **plan assets** and contributions to the plan expected to be made during the period. In estimating that rate, appropriate consideration should be given to the returns being earned on the plan assets currently invested and the rates of return expected to be available for reinvestment. If the return on plan assets is taxable to the trust or other fund under the plan, the expected long-term rate of return shall be reduced to reflect the related income taxes expected to be paid under existing law. The expected long-term rate of return on plan assets is used with the **market-related value of plan assets**

to compute the **expected return on plan assets.** (Refer to paragraph 57.) There is no assumption of an expected long-term rate of return on plan assets for plans that are unfunded or that have no assets that qualify as plan assets pursuant to this Statement.

33. The service cost component of net periodic postretirement benefit cost and the expected and accumulated postretirement benefit obligations shall reflect future compensation levels to the extent the postretirement benefit formula defines the benefits wholly or partially as a function of future compensation levels.[12] For pay-related plans, assumed compensation levels shall reflect the best estimate of the actual future compensation levels of the individual employees involved, including future changes attributed to general price levels, productivity, seniority, promotion, and other factors. All assumptions shall be consistent to the extent that each reflects expectations about the same future economic conditions, such as future rates of inflation. Measuring service cost and the expected and accumulated postretirement benefit obligations based on estimated future compensation levels entails considering any indirect effects, such as benefit limitations, that would affect benefits provided by the plan.[13]

Assumptions Unique to Postretirement Health Care Benefits

34. Measurement of an employer's postretirement health care obligation requires the use of several assumptions unique to health care benefits. Most significantly, it includes several assumptions about factors that will affect the amount and timing of future benefit payments for postretirement health care. Those factors include consideration of historical per capita claims cost by age, health care cost trend rates (for plans that provide a benefit in kind), and medical coverage to be paid by governmental authorities and other providers of health care benefits.

35. In principle, an employer's share of the expected future postretirement health care cost for a plan participant is developed by reducing the **assumed per capita claims cost** at each age at which the plan participant is expected to receive benefits under the plan by (a) the effects of coverage by Medicare and other providers of health care benefits, and (b) the effects of the cost-sharing provisions of the plan (deductibles, copayment provisions, out-of-pocket limitations, caps on the limits of the employer-provided payments, and retiree contributions).[14] The resulting amount represents the assumed **net incurred claims cost** at each age at which the plan participant is expected to receive benefits under the plan. If contributions are required to be paid by active plan participants toward their postretirement health care benefits, the actuarial present value of the plan participants' future contributions reduces the actuarial present value of the aggregate assumed net incurred claims costs.

36. The assumed per capita claims cost by age is the annual per capita cost, for periods after the measurement date, of providing the postretirement health care benefits covered by the plan from the earliest age at which an individual could begin to receive benefits under the plan through the remainder of the individual's life or the covered period, if shorter. The assumed per capita claims cost shall be the best estimate of the expected future cost of the benefits covered by the plan.[15] It may be appropriate to consider other factors in addition to age, such as sex and geographical location, in developing the assumed per capita claims cost.

37. Past and present claims data for the plan, such as a historical pattern of gross claims by age (claims curve), should be used in developing the current per capita claims cost to the extent that those data are considered to be indicative of the current cost of providing the benefits covered by the plan. Those current claims data shall be adjusted by the assumed health care cost trend rate. The resulting assumed per capita claims cost by age, together with the **plan demographics,** determines the amount and timing of expected future **gross eligible charges.**

38. In the absence of sufficiently reliable plan data about the current cost of the benefits covered by the plan, the current per capita claims cost should be based, entirely or in part, on the claims information of other employers to the extent those costs are indicative of the current cost of providing the benefits covered by the plan. For example, the current per capita claims cost may be based on the claims experience of other employers derived from information in data files developed by insurance companies, actuarial firms, or employee benefits consulting firms. The current per capita claims cost developed on those bases shall be adjusted to best reflect the terms of the employer's plan and the plan demographics. For example, the information should be adjusted, as necessary, for differing demographics, such as the age and sex of plan participants, health care utilization patterns by men and women at various ages, and the expected geographical location of retirees and their dependents, and for significant differences between the nature and types of benefits covered by the employer's plan and those encompassed by the underlying data.

39. The assumption about health care cost trend rates represents the expected annual rates of change in the cost of health care benefits currently provided by the postretirement benefit plan, due to factors other than changes in the demographics of the plan participants, for each year from the measurement date until the end of the period in which benefits are expected to be paid. Past and current health care cost trends shall be used in developing an employer's assumed health care cost trend rates, which implicitly consider estimates of health care inflation, changes in health care utilization or delivery patterns, technological advances, and changes in the health status of plan participants.[16] Differing services, such as hospital care and dental care, may require the use of different health care cost trend rates. It is appropriate for that assumption to reflect changes in health care cost trend rates over time. For example, the health care cost trend rates may be assumed to continue at the present level for the near term, or increase for a period of time, and then grade down over time to an estimated health care cost trend rate ultimately expected to prevail.

40. Certain medical claims may be covered by governmental programs under existing law or by other providers of health care benefits.[17] Benefit coverage by those governmental programs shall be assumed to continue as provided by the present law and by other providers pursuant to their present plans. Presently enacted changes in the law or amendments of the plans of other health care providers that take effect in future periods and that will affect the future level of their benefit coverage shall be considered in current-period measurements for benefits expected to be provided in those future periods. Future changes in laws concerning medical costs covered by governmental programs and future changes in the plans of other providers shall not be anticipated.

41. In some cases, determining the assumed per capita claims cost by age as described in paragraphs 36-38 may not be practical because credible historical information about the gross per capita cost of covered benefits may not be available or determinable to satisfy the stated measurement approach. However, credible historical information about **incurred claims costs** may be available. In those cases, an alternative method of developing the assumed per capita claims cost may be used provided the method results in a measure that is the best estimate of the expected future cost of the benefits covered by the plan. For example, the assumed health care cost trend rates may be determined by adjusting the expected change in the employer's share of per capita incurred claims cost by age by a factor that reflects the effects of the plan's cost-sharing provisions. However, an approach that projects net incurred claims costs using unadjusted assumed health care cost trend rates would implicitly assume changes in the plan's cost-sharing provisions at those assumed rates and, therefore, is not acceptable unless the plan's cost-sharing provisions are indexed in that manner or the substantive plan (paragraphs 24-26) operates in that manner.

42. Assumed discount rates include an inflationary element that reflects the expected general rate of inflation. Assumed compensation levels include consideration of future changes attributable to general price levels. Similarly, assumed health care cost trend rates include an element that reflects

expected general rates of inflation for the economy overall and an element that reflects price changes of health care costs in particular. To the extent that those assumptions consider similar inflationary effects, the assumptions about those effects shall be consistent.

Attribution

43. An equal amount of the expected postretirement benefit obligation for an employee generally shall be attributed to each year of service in the **attribution period** (a benefit/years-of-service approach). However, some plans may have benefit formulas that attribute a disproportionate share of the expected postretirement benefit obligation to employees' early years of service. For that type of plan, the expected postretirement benefit obligation shall be attributed in accordance with the plan's benefit formula.

44. The beginning of the attribution period generally shall be the date of hire. However, if the plan's benefit formula grants credit only for service from a later date and that **credited service period** is not nominal in relation to employees' total years of service prior to their full eligibility dates, the expected postretirement benefit obligation shall be attributed from the beginning of that credited service period. In all cases, the end of the attribution period shall be the full eligibility date. (Paragraphs 409-412 illustrate the attribution provisions of this Statement.)

Recognition of Net Periodic Postretirement Benefit Cost

45. As with other forms of deferred compensation, the cost of providing postretirement benefits shall be attributed to the periods of employee service rendered in exchange for those future benefits pursuant to the terms of the plan. That cost notionally represents the change in the **unfunded accumulated postretirement benefit obligation** for the period, ignoring employer contributions to the plan, plan settlements, and payments made by the employer directly to retirees. However, changes in that unfunded obligation that arise from experience gains and losses and the effects of changes in assumptions may be recognized as a component of net periodic postretirement benefit cost on a delayed basis. In addition, the effects of a plan initiation or amendment generally are recognized on a delayed basis.

46. The following components shall be included in the net postretirement benefit cost recognized for a period by an employer sponsoring a defined benefit postretirement plan:

a. Service cost (paragraph 47)
b. Interest cost (paragraph 48)
c. Actual return on plan assets, if any (paragraph 49)
d. Amortization of unrecognized prior service cost, if any (paragraphs 50-55)
e. **Gain or loss** (including the effects of changes in assumptions) to the extent recognized (paragraphs 56-62)
f. Amortization of the unrecognized obligation or asset existing at the date of initial application of this Statement, hereinafter referred to as the **unrecognized transition obligation** [18] or **unrecognized transition asset** (paragraphs 110 and 112).

Service Cost

47. The service cost component recognized in a period shall be determined as the portion of the expected postretirement benefit obligation attributed to employee service during that period. The measurement of the service cost component requires identification of the substantive plan and the use of assumptions and an attribution method, which are discussed in paragraphs 23-44.

Interest Cost

48. The interest cost component recognized in a period shall be determined as the increase in the accumulated postretirement benefit obligation to recognize the effects of the passage of time. Measuring the accumulated postretirement benefit obligation as a present value requires accrual of an interest cost at rates equal to the assumed discount rates.

Actual Return on Plan Assets

49. For a funded plan, the actual return on plan assets shall be determined based on the **fair value** of plan assets (refer to paragraphs 65 and 66) at the beginning and end of the period, adjusted for contributions and benefit payments. If the fund holding the plan assets is a taxable entity, the actual return on plan assets shall reflect the tax expense or benefit for the period determined in accordance with generally accepted accounting principles. Otherwise, no provision for taxes shall be included in the actual return on plan assets.

Prior Service Cost

50. Plan amendments (including initiation of a plan) may include provisions that attribute the increase or reduction in benefits to employee service rendered in prior periods or only to employee service to be rendered in future periods. For purposes of measuring the accumulated postretirement benefit obligation, the effect of a plan amendment on a plan participant's expected postretirement benefit obligation shall be attributed to each year of service in that plan participant's attribution period, including years of service already rendered by that plan participant, in accordance with the attribution of the expected postretirement benefit obligation to years of service as discussed in paragraphs 43 and 44. If a plan is initiated that grants benefits solely in exchange for employee service after the date of the plan initiation or a future date, no portion of the expected postretirement benefit obligation is attributed to prior service periods because, in that case, the credited service period for the current employees who are expected to receive benefits under the plan begins at the date of the plan initiation or the future date.

51. Plan amendments that improve benefits are granted with the expectation that the employer will realize economic benefits in future periods. Consequently, except as discussed in paragraph 54, this Statement does not permit the cost of benefit improvements (that is, prior service cost) to be included in net periodic postretirement benefit cost entirely in the year of the amendment. Rather, paragraph 52 provides for recognition of prior service cost arising from benefit improvements during the remaining years of service to the full eligibility dates of those plan participants active at the date of the plan amendment. (Refer to paragraph 55 for plan amendments that reduce benefits.)

52. The cost of benefit improvements (including improved benefits that are granted to **fully eligible plan participants**) is the increase in the accumulated postretirement benefit obligation as a result of the plan amendment, measured at the date of the amendment. Except as specified in the

next sentence and in paragraphs 53 and 54, that prior service cost shall be amortized by assigning an equal amount to each remaining year of service to the full eligibility date of each plan participant active at the date of the amendment who was not yet fully eligible for benefits at that date. If all or almost all of a plan's participants are fully eligible for benefits, the prior service cost shall be amortized based on the remaining life expectancy of those plan participants rather than on the remaining years of service to the full eligibility dates of the active plan participants.

53. To reduce the complexity and detail of the computations required, consistent use of an alternative amortization approach that more rapidly reduces unrecognized prior service cost is permitted. For example, a straight-line amortization of the cost over the average remaining years of service to full eligibility for benefits of the active plan participants is acceptable.

54. In some situations, a history of regular plan amendments and other evidence may indicate that the period during which the employer expects to realize economic benefits from an amendment that grants increased benefits is shorter than the remaining years of service to full eligibility for benefits of the active plan participants. Identification of those situations requires an assessment of the individual circumstances of the particular plan. In those circumstances, the amortization of prior service cost shall be accelerated to reflect the more rapid expiration of the employer's economic benefits and to recognize the cost in the periods benefited.

55. A plan amendment can reduce, rather than increase, the accumulated postretirement benefit obligation. A reduction in that obligation shall be used first to reduce any existing unrecognized prior service cost, then to reduce any remaining unrecognized transition obligation. The excess, if any, shall be amortized on the same basis as specified in paragraph 52 for prior service cost. Immediate recognition of the excess is not permitted.

Gains and Losses

56. Gains and losses are changes in the amount of either the accumulated postretirement benefit obligation or plan assets resulting from experience different from that assumed or from changes in assumptions. This Statement generally does not distinguish between those sources of gains and losses. Gains and losses include amounts that have been realized, for example, by the sale of a security, as well as amounts that are unrealized. Because gains and losses may reflect refinements in estimates as well as real changes in economic values and because some gains in one period may be offset by losses in another or vice versa, this Statement does not require recognition of gains and losses as components of net postretirement benefit cost in the period in which they arise, except as described in paragraph 61. (Gain and loss recognition in accounting for settlements and curtailments is addressed in paragraphs 90-99.)

57. The expected return on plan assets shall be determined based on the expected long-term rate of return on plan assets (refer to paragraph 32) and the market-related value of plan assets. The market-related value of plan assets shall be either fair value or a calculated value that recognizes changes in fair value in a systematic and rational manner over not more than five years. Different methods of calculating market-related value may be used for different classes of assets (for example, an employer might use fair value for bonds and a five-year-moving-average value for equities), but the manner of determining market-related value shall be applied consistently from year to year for each class of plan assets.

58. Plan asset gains and losses are differences between the actual return on plan assets during a period and the expected return on plan assets for that period. Plan asset gains and losses include both (a) changes reflected in the market-related value of plan assets and (b) changes not yet reflected in the market-related value of plan assets (that is, the difference between the fair value and the market-related value of plan assets). Plan asset gains and losses not yet reflected in market-related value are not required to be amortized under paragraphs 59 and 60.

59. As a minimum, amortization of an ♦**unrecognized net gain or loss** (excluding plan asset gains and losses not yet reflected in market-related value) shall be included as a component of net postretirement benefit cost for a year if, as of the beginning of the year, that unrecognized net gain or loss exceeds 10 percent of the greater of the accumulated postretirement benefit obligation or the market-related value of plan assets. If amortization is required, the minimum amortization [19] shall be that excess divided by the average remaining service period of active plan participants. If all or almost all of a plan's participants are inactive, the average remaining life expectancy of the inactive participants shall be used instead of the average remaining service period.

60. Any systematic method of amortization of unrecognized gains and losses may be used in place of the minimum amortization specified in paragraph 59 provided that (a) the minimum amortization is recognized in any period in which it is greater (reduces the unrecognized amount by more) than the amount that would be recognized under the method used, (b) the method is applied consistently, (c) the method is applied similarly to both gains and losses, and (d) the method used is disclosed. If an enterprise uses a method of consistently recognizing gains and losses immediately, any gain that does not offset a loss previously recognized in income pursuant to this paragraph shall first offset any unrecognized transition obligation; any loss that does not offset a gain previously recognized in income pursuant to this paragraph shall first offset any unrecognized transition asset.

61. In some situations, an employer may forgive a retrospective adjustment of the current or past years' cost-sharing provisions of the plan as they relate to benefit costs *already incurred* by retirees [20] or may otherwise deviate from the provisions of the substantive plan to increase or decrease the employer's share of the benefit costs *incurred in the current or past periods.* The effect of a decision to temporarily deviate from the substantive plan shall be immediately recognized as a loss or gain.

62. The gain or loss component of net periodic postretirement benefit cost shall consist of (a) the difference between the actual return on plan assets and the expected return on plan assets, (b) any gain or loss immediately recognized or the amortization of the unrecognized net gain or loss from previous periods, and (c) any amount immediately recognized as a gain or loss pursuant to paragraph 61.

Measurement of Plan Assets

63. Plan assets are assets-usually stocks, bonds, and other investments (except certain ♦**insurance contracts** as noted in paragraph 67)-that have been segregated and restricted (usually in a trust) to be used for postretirement benefits. The amount of plan assets includes amounts contributed by the employer, and by plan participants for a contributory plan, and amounts earned from investing the contributions, less benefits, income taxes, and other expenses incurred. Plan assets ordinarily cannot be withdrawn by the employer except under certain circumstances when a plan has assets in excess of obligations and the employer has taken certain steps to satisfy existing obligations. Securities of the employer held by the plan are includable in plan assets provided they are transferable.

64. Assets not segregated in a trust, or otherwise effectively restricted, so that they cannot be used by the employer for other purposes are not plan assets for purposes of this Statement, even though the employer may intend that those assets be used to provide postretirement benefits. Those assets shall be accounted for in the same manner as other employer assets of a similar nature and with similar restrictions. Amounts accrued by the employer but not yet paid to the plan are not plan assets for purposes of this Statement.

65. For purposes of the disclosures required by ~~paragraph 74~~, plan investments, whether equity or debt securities, real estate, or other, shall be measured at their fair value as of the measurement date. The fair value of an investment is the amount that the plan could reasonably expect to receive for it in a current sale between a willing buyer and a willing seller, that is, other than in a forced or liquidation sale. Fair value shall be measured by the market price if an active market exists for the investment. If no active market exists for an investment but an active market exists for similar investments, selling prices in that market may be helpful in estimating fair value. If a market price is not available, a forecast of expected cash flows may aid in estimating fair value, provided the expected cash flows are discounted at a current rate commensurate with the risk involved.[21] (Refer to paragraph 71.)

66. Plan assets used in plan operations (for example, buildings, equipment, furniture and fixtures, and leasehold improvements) shall be measured at cost less accumulated depreciation or amortization for all purposes.

Insurance Contracts

67. For purposes of this Statement, an insurance contract is defined as a contract in which an insurance company unconditionally undertakes a legal obligation to provide specified benefits to specific individuals in return for a fixed consideration or premium; an insurance contract is irrevocable and involves the transfer of significant risk from the employer (or the plan) to the insurance company.[22] Benefits covered by insurance contracts shall be excluded from the accumulated postretirement benefit obligation. Insurance contracts shall be excluded from plan assets, except as provided in paragraph 69 for the cost of **participation rights.**

68. Some insurance contracts (**participating insurance contracts**) provide that the purchaser (either the plan or the employer) may participate in the experience of the insurance company. Under those contracts, the insurance company ordinarily pays dividends to the purchaser, the effect of which is to reduce the cost of the plan. If the participating insurance contract causes the employer to remain subject to all or most of the risks and rewards associated with the benefit obligation covered or the assets transferred to the insurance company, that contract is not an insurance contract for purposes of this Statement, and the purchase of that contract does not constitute a settlement pursuant to paragraphs 90-95.

69. The purchase price of a participating insurance contract ordinarily is higher than the price of an equivalent contract without a participation right. The difference is the cost of the participation right. The cost of the participation right shall be recognized at the date of purchase as an asset. In subsequent periods, the participation right shall be measured at its fair value if the contract is such that fair value is reasonably estimable. Otherwise participation right shall be measured at its amortized cost (not in excess of its net realizable value), and the cost shall be amortized systematically over the expected dividend period under the contract.

70. To the extent that insurance contracts are purchased during the period to cover postretirement benefits attributed to service in the current period (such as life insurance benefits), the cost of those benefits shall be the cost of purchasing the coverage under the contracts, except as provided in paragraph 69 for the cost of a participation right. If all the postretirement benefits attributed to service in the current period are covered by **nonparticipating insurance contracts** purchased during that period, the cost of the contracts determines the service cost component of net postretirement benefit cost for that period. Benefits attributed to current service in excess of benefits provided by nonparticipating insurance contracts purchased during the current period shall be accounted for according to the provisions of this Statement applicable to plans not involving insurance contracts.

71. Other contracts with insurance companies may not meet the definition of an insurance contract because the insurance company does not unconditionally undertake a legal obligation to provide specified benefits to specified individuals. Those contracts shall be accounted for as investments and measured at fair value. If a contract has a determinable cash surrender value or conversion value, that is presumed to be its fair value. For some contracts, the best available estimate of fair value may be contract value.

Measurement Date

72. The measurements of *plan assets and obligations* required by this Statement shall be as of the date of the financial statements or, if used consistently from year to year, as of a date not more than three months prior to that date. Even though the postretirement benefit measurements are required as of a particular date, all procedures are not required to be performed after that date. As with other financial statement items requiring estimates, much of the information can be prepared as of an earlier date and projected forward to account for subsequent events (for example, employee service).

73. Measurements of *net periodic postretirement benefit cost* for both interim and annual financial statements generally shall be based on the assumptions at the beginning of the year (assumptions used for the previous year-end measurements of plan assets and obligations) unless more recent measurements of both plan assets and the accumulated postretirement benefit obligation are available. For example, if a significant event occurs, such as a plan amendment, settlement, or curtailment, that ordinarily would call for remeasurement, the assumptions used for those later measurements shall be used to remeasure net periodic postretirement benefit cost from the date of the event to the year-end measurement date.

~~Disclosures~~

~~74. This Statement requires disclosures about an employer's obligation to provide postretirement benefits and the cost of providing those benefits that are intended to enhance the usefulness of the financial statements to investors, creditors, and other users of financial information. An employer sponsoring one or more defined benefit postretirement plans (refer to paragraphs 77 and 78) shall disclose, if applicable, the following information about those plans:~~

~~a. A description of the substantive plan(s) that is the basis for the accounting (refer to paragraphs 23-28), including the nature of the plan, any modifications of the existing cost-sharing provisions that are encompassed by the substantive plan(s) (refer to paragraphs 24 and 25), and the existence and nature of any commitment to increase monetary benefits provided by the postretirement benefit plan (refer to paragraph 26), employee groups covered, types of benefits provided, **funding policy**, types of assets held and significant nonbenefit liabilities, and the nature and effect of significant matters affecting the comparability of information for all periods presented, such as the effect of a business combination or divestiture~~

~~b. The amount of net periodic postretirement benefit cost showing separately the service cost component, the interest cost component, the actual return on plan assets for the period, amortization of the unrecognized transition obligation or transition asset, and the net total of other components [23]~~

~~c. A schedule reconciling the funded status of the plan(s) with amounts reported in the employer's statement of financial position, showing separately:~~

~~(1) The fair value of plan assets~~

~~(2) The accumulated postretirement benefit obligation, identifying separately the portion attributable to retirees, other fully eligible plan and other active plan participants~~

~~(3) The amount of unrecognized prior service cost~~

~~(4) The amount of unrecognized net gain or loss (including plan asset gains and losses not yet reflected in market-related value)~~

~~(5) The amount of any remaining unrecognized transition obligation or transition asset~~

~~(6) The amount of net postretirement benefit asset or liability recognized in the statement of financial position, which is the net result of combining the preceding five items~~

~~d. The assumed health care cost trend rate(s) used to measure the expected cost of benefits covered by the plan (gross eligible charges) for the next year and a general description of the direction and pattern of change in the assumed trend rates thereafter, together with the ultimate trend rate(s) and when that rate is expected to be achieved~~

~~e. The weighted average of the assumed discount rate(s) and rate(s) of compensation increase (for pay-related plans) used to measure the accumulated postretirement benefit obligation and the weighted average of the expected long-term rate(s) of return on plan assets and, for plans whose income is segregated from the employer's investment income for tax purposes, the estimated income tax rate(s) included in that rate of return~~

~~f. The effect of a one-percentage-point increase in the assumed health care cost trend rates for each future year on (1) the aggregate of the service and interest cost components of net periodic postretirement health care benefit cost and (2) the accumulated postretirement benefit obligation for health care benefits (For purposes of this disclosure, all other assumptions shall be held constant and the effects shall be measured based on the substantive plan that is the basis for the accounting.)~~

~~g. The amounts and types of securities of the employer and related parties included in plan assets, and the approximate amount of future annual benefits of plan participants covered by insurance contracts issued by the employer and related parties~~

~~h. Any alternative amortization method used pursuant to paragraphs 53 or 60~~

~~i. The amount of gain or loss recognized during the period for a settlement or curtailment and a description of the nature of the event(s) (Refer to paragraphs 90-99.)~~

~~j. The cost of providing special or contractual termination benefits recognized during the period and a description of the nature of the event(s). (Refer to paragraphs 101 and 102.)~~

Employers with Two or More Plans

75. Postretirement benefits offered by an employer may vary in nature and may be provided to different groups of employees. As discussed in paragraph 76, in some cases an employer may aggregate data from unfunded plans for measurement purposes in lieu of performing separate measurements for each unfunded plan (including plans whose designated assets are not appropriately segregated and restricted and thus have no plan assets as that term is used in this Statement). Net periodic postretirement benefit cost, the accumulated postretirement benefit obligation, and plan assets shall be determined for each separately measured plan or aggregation of plans by applying the provisions of this Statement to each such plan or aggregation of plans.

76. The data from all unfunded postretirement health care plans may be aggregated for measurement purposes if (a) those plans provide different benefits to the same group of employees or (b) those plans provide the same benefits to different groups of employees. Data from other unfunded postretirement welfare benefit plans may be aggregated for measurement purposes in similar circumstances, such as when an employer has a variety of welfare benefit plans that provide benefits to the same group of employees. However, a plan that has plan assets (as defined herein) shall not be aggregated with other plans but shall be measured separately.

~~77. Disclosures for plans with plan assets in excess of the accumulated postretirement benefit obligation generally may be aggregated with disclosures for plans that have accumulated postretirement benefit obligations that exceed plan assets. However, for purposes of the disclosures required by paragraph 74(c), the aggregate plan assets and the aggregate accumulated postretirement benefit obligation of the underfunded plans shall be separately disclosed. Otherwise, except as described in paragraph 78, the disclosures required by this Statement may be aggregated for all of an employer's single-employer defined benefit plans, or plans may be disaggregated in groups to provide more useful information.~~

~~78. The disclosures required by this Statement shall be presented separately for the following:~~

~~a. Plans that provide primarily postretirement health care benefits and plans that provide primarily other postretirement welfare benefits if the accumulated postretirement benefit obligation of the latter plans is significant relative to the aggregate accumulated postretirement benefit obligation for all of the plans~~

~~b. Plans inside the United States and plans outside the United States if the accumulated postretirement benefit obligation of the latter plans is significant relative to the aggregate accumulated postretirement benefit obligation for all of the plans.~~

Multiemployer Plans

79. For purposes of this Statement, a **multiemployer plan** is a postretirement benefit plan to which two or more unrelated employers contribute, usually pursuant to one or more collective-bargaining agreements. A characteristic of multiemployer plans is that assets contributed by one participating employer may be used to provide benefits to employees of other participating employers since assets contributed by an employer are not segregated in a separate account or restricted to provide benefits only to employees of that employer.

80. A multiemployer plan usually is administered by a board of trustees composed of management and labor representatives and may also be referred to as a "joint trust" or "union plan." Generally, many employers participate in a multiemployer plan, and an employer may participate in more than one plan. The employers participating in multiemployer plans usually have a common industry bond, but for some plans the employers are in different

industries, and the labor union may be their only common bond. Some multiemployer plans do not involve a union. For example, local chapters of a not-for-profit organization may participate in a plan established by the related national organization.

81. An employer participating in a multiemployer plan shall recognize as net postretirement benefit cost the required contribution for the period, which shall include both cash and the fair market value of noncash contributions, and shall recognize as a liability any unpaid contributions required for the period.

~~82. An employer that participates in one or more multiemployer plans shall disclose the following separately from disclosures for a single-employer plan:~~

~~a. A description of the multiemployer plan(s) including the employee groups covered, the type of benefits provided (defined benefits or defined contribution), and the nature and effect of significant matters affecting comparability of information for all periods presented~~

~~b. The amount of postretirement benefit cost recognized during the period, if available. Otherwise, the amount of the aggregate required contribution for the period to the general health and welfare benefit plan that provides health and welfare benefits to both active employees and retirees shall be disclosed.~~

83. In some situations, withdrawal from a multiemployer plan may result in an employer's having an obligation to the plan for a portion of the plan's unfunded accumulated postretirement benefit obligation. If it is either probable or reasonably possible that (a) an employer would withdraw from the plan under circumstances that would give rise to an obligation or (b) an employer's contribution to the fund would be increased during the remainder of the contract period to make up a shortfall in the funds necessary to maintain the negotiated level of benefit coverage (a "maintenance of benefits" clause), the employer shall apply the provisions of FASB Statement No. 5, *Accounting for Contingencies.*

Multiple-Employer Plans

84. Some postretirement benefit plans to which two or more unrelated employers contribute are not multiemployer plans. Rather, those **multiple-employer plans** are in substance aggregations of single-employer plans, combined to allow participating employers to pool plan assets for investment purposes or to reduce the costs of plan administration. Those plans ordinarily do not involve collective-bargaining agreements. They may also have features that allow participating employers to have different benefit formulas, with the employer's contributions to the plan based on the benefit formula selected by the employer. Those plans shall be considered single-employer plans rather than multiemployer plans for purposes of this Statement, and each employer's accounting shall be based on its respective interest in the plan.

Postretirement Benefit Plans outside the United States

85. Except for its effective date (paragraph 108), this Statement includes no special provisions applicable to postretirement benefit arrangements outside the United States. Those arrangements are subject to the provisions of this Statement for purposes of preparing financial statements in accordance with accounting principles generally accepted in the United States. The applicability of this Statement to those arrangements is determined by the nature of the obligation and by the terms or conditions that define the amount of benefits to be paid, not by whether or how a plan is funded, whether benefits are payable at intervals or as a single amount, or whether the benefits are required by law or custom or are provided under a plan the employer has elected to sponsor.

Business Combinations

86. When an employer is acquired in a business combination ~~that is accounted for by the purchase method under Opinion 16~~ and that employer sponsors a single-employer defined benefit postretirement plan, the assignment of the purchase price to individual assets acquired and liabilities assumed shall include a liability for the accumulated postretirement benefit obligation in excess of the fair value of the plan assets or an asset for the fair value of the plan assets in excess of the accumulated postretirement benefit obligation. The accumulated postretirement benefit obligation assumed shall be measured based on the benefits attributed by the acquired entity to employee service prior to the date the business combination is consummated, adjusted to reflect (a) any changes in assumptions based on the purchaser's assessment of relevant future events (as discussed in paragraphs 23-42) and (b) the terms of the substantive plan (as discussed in paragraphs 23-28) to be provided by the purchaser to the extent they differ from the terms of the acquired entity's substantive plan.

87. If the postretirement benefit plan of the acquired entity is amended as a condition of the business combination (for example, if the change is required by the seller as part of the consummation of the acquisition), the effects of any improvements attributed to services rendered by the participants of the acquired entity's plan prior to the date of the business combination shall be accounted for as part of the accumulated postretirement benefit obligation of the acquired entity. Otherwise, if improvements to the postretirement benefit plan of the acquired entity are not a condition of the business combination, credit granted for prior service shall be recognized as a plan amendment as discussed in paragraphs 50-55. If it is expected that the plan will be terminated or curtailed, the effects of those actions shall be considered in measuring the accumulated postretirement benefit obligation. Otherwise, no future changes to the plan shall be anticipated.

88. As a result of applying the provisions of paragraphs 86 and 87, any previously existing unrecognized net gain or loss, unrecognized prior service cost, or unrecognized transition obligation or transition asset is eliminated for the acquired employer's plan. Subsequently, to the extent that the net obligation assumed or net assets acquired are considered in determining the amounts of contributions to the plan, differences between the purchaser's net periodic postretirement benefit cost and amounts it contributes will reduce the liability or asset recognized at the date of the combination.

Amendment to Opinion 16

89. The following footnote is added to the end of the last sentence of paragraph 88 of Opinion 16:

> *Paragraphs 86-88 of FASB Statement No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions,* specify how the general guidelines of this paragraph shall be applied to assets and liabilities related to plans that provide postretirement benefits other than pensions.

Accounting for Settlement of a Postretirement Benefit Obligation

90. For purposes of this Statement, a settlement is defined as a transaction that (a) is an irrevocable action, (b) relieves the employer (or the plan) of primary responsibility for a postretirement benefit obligation, and (c) eliminates significant risks related to the obligation and the assets used to effect the

settlement.[24] Examples of transactions that constitute a settlement include making lump-sum cash payments to plan participants in exchange for their rights to receive specified postretirement benefits and purchasing long-term nonparticipating insurance contracts for the accumulated postretirement benefit obligation for some or all of the plan participants.

91. A transaction that does not meet the three criteria of paragraph 90 does not constitute a settlement for purposes of this Statement. For example, investing in a portfolio of high-quality fixed-income securities with principal and interest payment dates similar to the estimated payment dates of benefits may avoid or minimize certain risks. However, that investment decision does not constitute a settlement because that decision can be reversed, and investing in that portfolio does not relieve the employer (or the plan) of primary responsibility for a postretirement benefit obligation nor does it eliminate significant risks related to that obligation.

92. For purposes of this Statement, the maximum gain or loss subject to recognition in income when a postretirement benefit obligation is settled is the unrecognized net gain or loss defined in paragraphs 56-60 plus any remaining unrecognized transition asset. That maximum gain or loss includes any gain or loss resulting from remeasurements of plan assets and the accumulated postretirement benefit obligation at the time of settlement.

93. If the entire accumulated postretirement benefit obligation is settled and the maximum amount subject to recognition is a gain, the settlement gain shall first reduce any remaining unrecognized transition obligation; [25] any excess gain shall be recognized in income.[26] If the entire accumulated postretirement benefit obligation is settled and the maximum amount subject to recognition is a loss, the maximum settlement loss shall be recognized in income. If only part of the accumulated postretirement benefit obligation is settled, the employer shall recognize in income the excess of the pro rata portion (equal to the percentage reduction in the accumulated postretirement benefit obligation) of the maximum settlement gain over any remaining unrecognized transition obligation or a pro rata portion of the maximum settlement loss.

94. If the purchase of a participating insurance contract constitutes a settlement (refer to paragraphs 67 and 90), the maximum gain (but not the maximum loss) shall be reduced by the cost of the participation right before determining the amount to be recognized in income.

95. If the cost of all settlements [27] in a year is less than or equal to the sum of the service cost and interest cost components of net postretirement benefit cost for the plan for the year, gain or loss recognition is permitted but not required for those settlements. However, the accounting policy shall be applied consistently from year to year.

Accounting for a Plan Curtailment

96. For purposes of this Statement, a curtailment is an event that significantly reduces the expected years of future service of active plan participants or eliminates the accrual of defined benefits for some or all of the future services of a significant number of active plan participants. Curtailments include:

a. Termination of employees' services earlier than expected, which may or may not involve closing a facility or discontinuing a ~~segment of a business~~

b. Termination or suspension of a plan so that employees do not earn additional benefits for future service. In the latter situation, future service may be counted toward eligibility for benefits accumulated based on past service.

97. The unrecognized prior service cost associated with the portion of the future years of service that had been expected to be rendered, but as a result of a curtailment are no longer expected to be rendered, is a loss. For purposes of measuring the effect of a curtailment, unrecognized prior service cost includes the cost of plan amendments and any remaining unrecognized transition obligation. For example, a curtailment may result from the termination of a significant number of employees who were plan participants at the date of a prior plan amendment.[28] The loss associated with that curtailment is measured as (a) the portion of the remaining unrecognized prior service cost related to that (and any prior) plan amendment attributable to the previously expected remaining future years of service of the employees who were terminated and (b) the portion of the remaining unrecognized transition obligation attributable to the previously expected remaining future years of service of the terminated employees who were plan participants at the date of transition.

98. The accumulated postretirement benefit obligation may be decreased (a gain) or increased (a loss) by a curtailment. [29] That (gain) loss shall reduce any unrecognized net loss (gain).

a. To the extent that such a gain exceeds any unrecognized net loss (or the entire gain, if an unrecognized net gain exists), it is a curtailment gain.

b. To the extent that such a loss exceeds any unrecognized net gain (or the entire loss, if an unrecognized net loss exists), it is a curtailment loss.

For purposes of applying the provisions of this paragraph, any remaining unrecognized transition asset shall be treated as an unrecognized net gain and shall be combined with the unrecognized net gain or loss arising subsequent to transition to this Statement.

99. If the sum of the effects identified in paragraphs 97 and 98 is a net loss, it shall be recognized in income when it is probable that a curtailment will occur and the net effect is reasonably estimable. If the sum of those effects is a net gain, it shall be recognized in income when the related employees terminate or the plan suspension or amendment is adopted.

Relationship of Settlements and Curtailments to Other Events

100. A settlement and a curtailment may occur separately or together. If benefits expected to be paid in future periods are eliminated for some plan participants (for example, because a significant portion of the work force is dismissed or a plant is closed) but the plan remains in existence and continues to pay benefits, to invest assets, and to receive contributions, a curtailment has occurred but not a settlement. If an employer purchases nonparticipating insurance contracts for the accumulated postretirement benefit obligation and continues to provide defined benefits for future service, either in the same plan or in a successor plan, a settlement has occurred but not a curtailment. If a **plan termination** occurs (that is, the obligation is settled and the plan ceases to exist) and the plan is not replaced by a successor defined benefit plan, both a settlement and a curtailment have occurred (whether or not the employees continue to work for the employer).

Measurement of the Effects of Termination Benefits

101. Postretirement benefits offered as special or contractual termination benefits shall be recognized in accordance with paragraph 15 of Statement

88. That is, an employer that offers special termination benefits to employees shall recognize a liability and a loss when the employees accept the offer and the amount can be reasonably estimated. An employer that provides contractual termination benefits shall recognize a liability and a loss when it is probable that employees will be entitled to benefits and the amount can be reasonably estimated. A situation involving special or contractual termination benefits may also result in a curtailment to be accounted for under paragraphs 96-99 of this Statement.

102. The liability and loss recognized for employees who accept an offer of special termination benefits to be provided by a postretirement benefit plan shall be the difference between (a) the accumulated postretirement benefit obligation for those employees, assuming that those employees (active plan participants) not yet fully eligible for benefits would terminate at their full eligibility date and that fully eligible plan participants would retire immediately, without considering any special termination benefits and (b) the accumulated postretirement benefit obligation as measured in (a) adjusted to reflect the special termination benefits.

Disposal of a Segment

103. If the gain or loss measured in accordance with paragraphs 92-94, 97-99, or 101 and 102 is directly related to disposal of a segment of a business ~~or a portion of a line of business~~, it shall be included in determining the gain or loss associated with that event. The net gain or loss attributable to the disposal shall be recognized pursuant to the requirements of APB Opinion No. 30, *Reporting the Results of Operations-Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions.*

Defined Contribution Plans

104. For purposes of this Statement, a **defined contribution postretirement plan** is a plan that provides postretirement benefits in return for services rendered, provides *an individual account* for each participant, and has terms that specify how contributions to the individual's account are to be determined rather than the amount of postretirement benefits the individual is to receive.[30] Under a defined contribution plan, the postretirement benefits a plan participant will receive are limited to the amount contributed to the plan participant's account, the returns earned on investments of those contributions, and forfeitures of other plan participants' benefits that may be allocated to the plan participant's account.

105. To the extent a plan's defined contributions to an individual's account are to be made for periods in which that individual renders services, the net postretirement benefit cost for a period shall be the contribution called for in that period. If a plan calls for contributions for periods after an individual retires or terminates, the estimated cost shall be accrued during the employee's service period.

~~106. An employer that sponsors one or more defined contribution plans shall disclose the following separately from its defined benefit plan disclosures:~~

~~a. A description of the plan(s) including employee groups covered, the basis for determining contributions, and the nature and effect of significant matters affecting comparability of information for all periods presented~~

~~b. The amount of cost recognized during the period.~~

107. A postretirement benefit plan having characteristics of both a defined benefit plan and a defined contribution plan requires careful analysis. If the *substance* of the plan is to provide a defined benefit, as may be the case with some "target benefit" plans, the accounting ~~and disclosure shall be determined in accordance with the provisions of this Statement applicable to a defined benefit plan~~.

Effective Dates and Transition

108. Except as noted in the following sentences of this paragraph and in paragraphs 114 and 115, this Statement shall be effective for fiscal years beginning after December 15, 1992. For plans outside the United States and for defined benefit plans of employers that (a) are **nonpublic enterprises** and (b) sponsor defined benefit postretirement plan(s) with no more than 500 plan participants in the aggregate, this Statement shall be effective for fiscal years beginning after December 15, 1994. Earlier application is encouraged. Restatement of previously issued annual financial statements is not permitted. If a decision is made in other than the first interim period of an employer's fiscal year to apply this Statement early, previous interim periods of that year shall be restated.

109. If at the transition date an employer has excluded assets in a **postretirement benefit fund** from its statement of financial position and some or all of the assets in that fund do not qualify as plan assets as defined herein, the employer shall recognize in the statement of financial position the fair value of those nonqualifying assets as the employer's assets (not prepaid postretirement benefit cost) and an equal amount as an accrued postretirement benefit obligation pursuant to the transition to this Statement and before applying paragraph 110. Thereafter, those assets shall be accounted for in accordance with generally accepted accounting principles applicable to those types of assets, including their presentation in the employer's statement of financial position based on any restrictions on their use. The fair value of those assets at the transition date shall be used as their cost.

110. For a defined benefit plan, an employer shall determine as of the measurement date (paragraph 72) for the beginning of the fiscal year in which this Statement is first applied (the transition date), the amounts of (a) the accumulated postretirement benefit obligation and (b) the fair value of plan assets plus any recognized accrued postretirement benefit cost or less any recognized prepaid postretirement benefit cost. The difference between those two amounts, whether it represents a transition obligation or a transition asset, may be recognized either immediately in net income of the period of the change (paragraph 111) as the effect of a change in accounting principle, [31] or on a delayed basis (paragraph 112) as a component of net periodic postretirement benefit cost. Any transition obligation related to a defined contribution plan shall be recognized in the same manner. A single method of transition shall be elected at the date this Statement is initially applied for all defined benefit and defined contribution postretirement plans.

111. If immediate recognition of the transition obligation or asset is elected, the amount attributable to the effects of a plan initiation or any benefit improvements adopted after December 21, 1990 shall be treated as unrecognized prior service cost and excluded from the transition amount immediately recognized. In addition, an employer who chooses to immediately recognize the transition obligation or asset shall, at the date of transition, adjust as necessary the accounting for purchase business combinations consummated subsequent to December 21, 1990 to include in the assignment of the purchase price to assets acquired and liabilities assumed, recognition of the difference between the accumulated postretirement benefit and the fair value of the plan assets, as described in paragraphs 87 and 88. If reliable information on which to base measurement of the assumed postretirement benefit obligation as of the date the business combination is consummated is not available, the purchaser shall retroactively adjust the purchase price allocation to recognize the obligation assumed or the asset acquired, using the best information available at the date of transition to this Statement. The cumulative effect on prior periods' income of that retroactive adjustment of the purchase price allocation, for example, increased

amortization of goodwill associated with the business combination, and the amortization of prior service cost related to a plan initiation or amendment adopted after December 21, 1990, shall be recognized as part of the effect of the accounting change to adopt this Statement.

112. If delayed recognition is elected, the transition obligation or asset shall be amortized on a straight-line basis over the average remaining service period of active plan participants, except that (a) if the average remaining service period is less than 20 years, the employer may elect to use a 20-year period, and (b) if all or almost all of the plan participants are inactive, the employer shall use the average remaining life expectancy period of those plan participants. However, amortization of the transition obligation shall be accelerated if the cumulative benefit payments subsequent to the transition date to all plan participants exceed the cumulative postretirement benefit cost accrued subsequent to the transition date. In that situation, an additional amount of the unrecognized transition obligation shall be recognized equal to the excess cumulative benefit payments. For purposes of applying this provision, cumulative benefit payments shall be reduced by any plan assets or any recognized accrued postretirement benefit obligation at the transition date. Payments made pursuant to a settlement, as discussed in paragraphs 90-94, shall be included in the determination of cumulative benefit payments made subsequent to the transition date.

113. If at the measurement date for the beginning of an employer's fiscal year it is expected that additional recognition of any remaining unrecognized transition obligation will be required pursuant to paragraph 112, amortization of the transition obligation for interim reporting purposes shall be based on the amount expected to be amortized for the year, except for the effects of applying paragraph 112 for any settlement required to be accounted for pursuant to paragraphs 90-94. Those effects shall be recognized when the related settlement is recognized. The effects of changes during the year in the initial assessment of whether additional recognition of the unrecognized transition obligation will be required for the year shall be recognized over the remainder of the year. The amount of the unrecognized transition obligation to be recognized for a year shall be finally determined at the measurement date for the end of the year based on the constraints on delayed recognition discussed in paragraph 112; any difference between the amortization of the transition obligation recognized during interim periods and the amount required to be recognized for the year shall be recognized immediately.

Effective Date and Transition-Amendment to Opinion 12

114. Paragraph 6 and the related footnote of APB Opinion No. 12, *Omnibus Opinion-1967,* are amended effective for fiscal years beginning after March 15, 1991. The effect of the amendment on existing individual deferred compensation contracts, other than those providing postretirement health or welfare benefits, shall be recognized as the effect of a change in accounting principle in accordance with paragraphs 17-21 of APB Opinion No. 20, *Accounting Changes.* Individual deferred compensation contracts that provide postretirement health or welfare benefits shall be subject to the general transition provisions and effective dates of this Statement.

Rescission of Technical Bulletin 87-1

115. Effective with the issuance of this Statement, FASB Technical Bulletin No. 87-1, *Accounting for a Change in Method of Accounting for Certain Postretirement Benefits,* is rescinded. If a change in method of accounting for postretirement benefits is adopted subsequent to the issuance of this Statement, the new method shall comply with the provisions of this Statement.

The provisions of this Statement need not be applied to immaterial items.

This Statement was adopted by the unanimous vote of the seven members of the Financial Accounting Standards Board:

Dennis R. Beresford, *Chairman*
Victor H. Brown
Raymond C. Lauver
James J. Leisenring
C. Arthur Northrop
A. Clarence Sampson
Robert J. Swieringa

Notes to FAS 106

Note 1
Words that appear in the glossary are set in **boldface type** the first time they appear.

Note 2
The accounting for benefits paid after employment but before retirement (for example, layoff benefits) is a separate phase of the Board's project on accounting for postemployment benefits other than pensions. The fact that this Statement does not apply to those benefits should not be construed as discouraging the use of accrual accounting for those benefits.

Note 3
This Statement uses the term *net periodic postretirement benefit cost* rather than *net postretirement benefit expense* because part of the cost recognized in a period may be capitalized along with other costs as part of an asset such as inventory.

Note 4
The determination of disability benefits to be accrued pursuant to this Statement is based on the terms of the postretirement benefit plan defining when a disabled employee is entitled to postretirement benefits.

Note 5
Postretirement health care benefits are likely to be the most significant in terms of cost and prevalence, and certain of the issues that arise in measuring those benefits are unique. Therefore, much of the language of this Statement focuses on postretirement health care plans. Nevertheless, this Statement applies equally to all postretirement benefits.

Note 6
Two Special Reports prepared by the FASB staff, *A Guide to Implementation of Statement 87 on Employers' Accounting for Pensions,* and *A Guide to Implementation of Statement 88 on Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits,* provide accounting guidance on implementation questions raised in connection with Statements 87 and 88. Many of the provisions in this Statement are the same as or are similar to the provisions of Statements 87 and 88. Consequently, the guidance provided in those Special Reports should be useful in understanding and implementing many of the provisions of this Statement.

Note 7
The accumulated postretirement benefit obligation generally reflects a ratable allocation of expected future benefits to employee service already rendered in the attribution period; the accumulated benefit obligation under Statement 87 generally reflects the future benefits allocated to employee service in accordance with the benefit formula. In addition, unlike Statement 87, this Statement implicitly considers salary progression in the measurement of the accumulated postretirement benefit obligation of a pay-related plan.

Note 8
The interest cost component of postretirement benefit cost shall not be considered interest for purposes of applying FASB Statement No. 34, *Capitalization of Interest Cost.*

Note 9
For example, a past practice of increasing retiree contributions annually based on a specified index or formula may appear to indicate that the substantive plan includes a determinable indexing of the retirees' annual contributions to the plan. However, if that past practice of increasing retiree contributions is accompanied by identifiable offsetting changes in other benefits or compensation, those offsetting changes would indicate that the substantive plan incorporates only the *current* cost-sharing provisions. Therefore, future increases or reductions of those cost-sharing provisions should not be incorporated in measuring the expected postretirement benefit obligation.

Note 10
By definition, an employer does not have the unilateral right to change a collectively bargained plan. Therefore, if the postretirement benefits are the subject of collective bargaining, the extant written plan shall be the substantive plan unless the employer can demonstrate its ability to maintain (a) a consistent level of cost sharing or (b) a consistent practice of increasing or reducing its share of the cost of the covered benefits in past negotiations without making offsetting changes in other benefits or compensation of the affected plan participants or by incurring other significant costs to maintain that cost-sharing arrangement.

Note 11
For purposes of this Statement, a plan that promises to provide retirees a benefit in kind, such as health care benefits, rather than a defined dollar amount of benefit, is considered to be a plan that specifies automatic benefit changes. (The assumed rate of change in the future cost of providing health care benefits, the assumed health care cost trend rate, is discussed in paragraph 39.) Because automatic benefit changes are not conditional on employees rendering additional years of service, the full eligibility date is not affected by those changes. A benefit in kind includes the direct rendering of services, the payment directly to others who provide the services, or the reimbursement of the retiree's payment for those services.

Note 12
For pay-related plans, salary progression is included in measuring the expected postretirement benefit obligation. For example, a postretirement health care plan may define the deductible amount or copayment, or a postretirement life insurance plan may define the amount of death benefit, based on the employee's average or final level of annual compensation.

Note 13
For example, a plan may define the maximum benefit to be provided under the plan (a fixed cap). In measuring the expected postretirement benefit obligation under that plan, the projected benefit payments would be limited to that cap. For a plan that automatically adjusts the maximum benefit to be provided under the plan for the effects of inflation (an adjustable cap), the expected postretirement benefit obligation would be measured based on adjustments to that cap consistent with the assumed inflation rate reflected in other inflation-related assumptions.

Note 14
In some cases, retiree contributions are established based on the average per capita cost of benefit coverage under an employer's health care plan that provides coverage to both active employees and retirees. However, the medical cost of the retirees may cause the average per capita cost of benefit coverage under the plan to be higher than it would be if only active employees were covered by the plan. In that case, the employer has a postretirement benefit obligation for the portion of the expected future cost of the retiree health care benefits that are not recovered through retiree contributions, Medicare, or other providers of health care benefits.

Note 15
If significant, the internal and external costs directly associated with administering the postretirement benefit plan also should be accrued as a component of assumed per capita claims cost.

Note 16
An assumption about changes in the health status of plan participants considers, for example, the probability that certain claims costs will be incurred based on expectations of future events, such as the likelihood that some retirees will incur claims requiring technology currently being developed or that historical claims experience for certain medical needs may be reduced as a result of participation in a wellness program.

Note 17
For example, a retiree's spouse also may be covered by the spouse's present (or former) employer's health care plan. In that case, the spouse's employer (or former employer) may provide either primary or secondary postretirement health care benefits to the retiree's spouse or dependents.

Note 18
Amortization of the unrecognized transition obligation or asset will be adjusted prospectively to recognize the effects of (a) a negative plan amendment pursuant to paragraph 55, (b) a constraint on immediate recognition of a net gain or loss pursuant to paragraph 60, (c) settlement accounting pursuant to paragraphs 92 and 93, (d) plan curtailment accounting pursuant to paragraphs 97-99, and (e) a constraint on delayed recognition of the unrecognized transition obligation pursuant to paragraph 112.

Note 19
The amortization must always reduce the beginning-of-the-year balance. Amortization of an unrecognized net gain results in a decrease in net periodic postretirement benefit cost; amortization of an unrecognized net loss results in an increase in net periodic postretirement benefit cost.

Note 20
For example, the terms of a substantive postretirement health care plan may provide that any shortfall resulting from current year benefit payments in excess of the employer's stated share of incurred claims cost and retiree contributions for that year is to be recovered from increased retiree contributions in the subsequent year. The employer may subsequently determine that increasing retiree contributions for the shortfall in the prior year would be onerous and make a decision to bear the cost of the shortfall for that year. The employer's decision to bear the shortfall represents a change in intent and the resulting loss shall be recognized immediately. Future decisions by the employer to continue to bear the shortfall suggest an amendment of the substantive plan that should be accounted for as described in paragraphs 50-55.

Note 21
For an indication of factors to be considered in determining the discount rate, refer to paragraphs 13 and 14 of APB Opinion No. 21, *Interest on Receivables and Payables*. If significant, the fair value of an investment shall reflect the brokerage commissions and other costs normally incurred in a sale.

Note 22
If the insurance company providing the contract does business primarily with the employer and related parties (a **captive insurer**) or if there is any reasonable doubt that the insurance company will meet its obligations under the contract, the contract is not an insurance contract for purposes of this Statement.

Note 23
~~The net total of other components is generally the net effect during the period of certain delayed recognition provisions of this Statement. That net total includes:~~

~~a. The net asset gain or loss during the period deferred for later recognition (in effect, an offset or a supplement to the actual return on plan assets)~~

~~b. Amortization of unrecognized prior service cost~~

~~c. Amortization of the net gain or loss from earlier periods~~

d. Any gain or loss recognized due to a temporary deviation from the substantive plan (paragraph 61).

Note 24
If an insurance contract is purchased from an insurance company controlled by the employer, the purchase of the contract does not constitute a settlement.

Note 25
As discussed in paragraph 112, in measuring the gain or loss subject to recognition in income when a postretirement benefit obligation is settled, it shall first be determined whether recognition of an additional amount of any unrecognized transition obligation is required.

Note 26
Because the plan is the unit of accounting, the determination of the effects of a settlement considers only the unrecognized net gain or loss and unrecognized transition obligation or asset related to the plan for which all or a portion of the accumulated postretirement benefit obligation is being settled. Note 27
For the following types of settlements, the cost of the settlement is:

a. For a cash settlement, the amount of cash paid to plan participants

b. For a settlement using nonparticipating insurance contracts, the cost of the contracts

c. For a settlement using participating insurance contracts, the cost of the contracts less the amount attributed to participation rights. (Refer to paragraphs 68 and 69.)

Note 28
A curtailment also may result from terminating the accrual of additional benefits for the future services of a significant number of employees. The loss in that situation is (a) a proportionate amount of the remaining unrecognized prior service cost based on the portion of the remaining expected years of service in the amortization period that originally was attributable to those employees who were plan participants at the date of the plan amendment and whose future accrual of benefits has been terminated and (b) a proportionate amount of the remaining unrecognized transition obligation based on the portion of the remaining years of service of all participants active at the date of transition that originally was attributable to the remaining expected future years of service of the employees whose future accrual of benefits has been terminated.

Note 29
Increases in the accumulated postretirement benefit obligation that reflect termination benefits are excluded from the scope of this paragraph. (Refer to paragraphs 101 and 102.)

Note 30
For example, an employer may establish individual postretirement health care accounts for each employee, each year contributing a specified amount to each active employee's account. The balance in each employee's account may be used by that employee after the employee's retirement to purchase health care insurance or for other health care benefits. Rather than providing for defined health care benefits, the employer is providing a defined amount of money that may be used by retirees toward the payment of their health care costs.

Note 31
The effect of the accounting change and the related income tax effect shall be presented in the statement of income between the captions "extraordinary items" and "net income." The per share information presented on the statement of income shall include the per share effect of the accounting change.

Information Request AG-1-49

Please provide the current cost of equity capital for each of the Companies. Please also provide the workpapers, calculations, formulas, assumptions, and supporting documentation for each determination.

Response

The Department has set the cost of equity for each Company in rate proceedings. The current cost of equity capital for each distribution company is the last Department-approved cost of equity as follows: Boston Edison, 11.75 percent (per the cost of service used to set the cast-off rates in Boston Edison's restructuring settlement agreement in D.P.U./D.T.E. 96-23); Cambridge, 9.9 percent (per the return on the fixed component established in D.P.U./D.T.E. 97-111); Commonwealth, 10.8 percent (per the return on the fixed component established in D.P.U./D.T.E. 97-111); and NSTAR Gas Company, 13 percent (D.P.U. 91-60).

Information Request AG-1-52

Referring to the proposed Tariffs, page 3, Section 1.05, please provide a complete and detailed description of the methodology that the Company will use to determine the amount of deferred taxes included in the DTA. Please also provide an example of those calculations for year-end 2002, along with all workpapers, calculations, formulas, assumptions, and supporting calculations.

Response

Please refer to the Company's response to Information Request DTE-2-19 for a description of the deferred taxes included in the PAM. Please see also the response to Information Request AG-1-53.

Information Request AG-1-53

Referring to the proposed Tariffs, page 3, Section 1.05, please provide a complete and detailed description of the reasons for using the Deferred Tax Amount on the year-end Pre-Paid Amount when the APPA apparently uses the year-average Pre-Paid Amount.

Response

The deferred taxes on the pre-paid amount are calculated based on the average balance rather than the year-end balance of the pre-paid pension balance. Please refer to the Company's response to Information Request DTE-2-19 for an illustrative calculation of deferred taxes.

With respect to the Tariffs, page 3, Section 1.05, the sentence should be revised to read "The Deferred Tax Amount is the deferred taxes associated with (i) the average Pre-Paid Amount and (ii) the URD at the end of the Prior Year." rather than "The Deferred Tax Amount is the deferred taxes associated with the Pre-Paid Amount and the URD at the end of the Prior Year."

Information Request AG-1-57

Referring to the proposed Tariffs, page 3, Section 1.07, please provide an example of the Customer Notification that the Company proposes to use based on each Company's response to Information Request AG-1-56.

Response

For the reasons explained in the Company's response to Information Request DTE-2-8, it is not possible to compute the precise amount of the PAF for each company at this time. However, Attachment AG-1-57 is a format for the Customer Notification. The amounts would be inserted after the Department approval of the PAF.

Customer Notification

January Message On Billing Statements:

THIS BILL REFLECTS 2004 RATE CHANGES AS FOLLOWS (CENTS PER KWH): THE TRANSITION CHARGE HAS DECREASED TO X.XXX, THE RENEWABLE ENERGY CHARGE HAS DECREASED TO X.XXX, AND THE TRANSMISSION CHARGE HAS DECREASED TO X.XXX. THIS BILL ALSO INCLUDES AN ADJUSTABLE CHARGE TO RECOVER THE ANNUAL CHANGE FOR THE COSTS FOR PENSIONS AND OTHER POST RETIREMENT BENEFITS. IF YOUR BILL REFLECTS USAGE BEFORE JAN.1, IT HAS BEEN PRORATED.

Language for bill insert "2004 Electric Rates" to be distributed with customer bills in 2004.

Rates include an adjustable charge of x.xxx cents/kWh approved by the Department of Telecommunications and Energy effective January 1, 2004. This charge helps recover the annual change for the cost of pensions and other post-retirement benefits.